

BEFORE THE  
NEBRASKA PUBLIC SERVICE COMMISSION

In the Matter of the Application of	)	Case No. NG-0031
Aquila, Inc., d/b/a Aquila Networks	)	
(Aquila), Omaha, seeking authority	)	
for Limited Cost Recovery in the	)	
State of Nebraska	)	

**PRE-HEARING BRIEF OF THE PUBLIC ADVOCATE**

On August 1, 2005, Aquila, Inc., d/b/a Aquila Networks (“Aquila”) filed its “Application of Aquila Inc d/b/a Aquila Networks for Limited Cost Recovery” (the “Application”). On August 26, 2005, the Public Advocate filed a Petition for Formal Intervention. Cornerstone Energy also filed a Petition for Formal Intervention on August 23, 2005. On September 7, 2005, the Commission entered its Order Granting Petition for Intervention, which granted both Petitions for Formal Intervention.

On September 9, 2005, Commissioner Landis, as Hearing Officer, entered a Planning Conference Order dividing this proceeding into two phases. Phase I is to address the threshold question of whether Aquila’s Application is permissible under existing statutes and consistent with public policy considerations. Phase II, which would address the merits of Aquila’s Application, will only proceed if the Commission determines in Phase I that Aquila’s Application is both permissible under existing statutes and consistent with public policy considerations.

The September 9, 2005 Planning Conference Order also provided a deadline for the parties to file initial briefs by the close of business on October 7, 2005 and further

provided that each party shall have an opportunity to file reply briefs by the close of business on October 17, 2005. This brief is respectfully submitted by the Public Advocate as its initial brief in this matter. The Public Advocate will address legal issues and public policy issues separately below under appropriate argument headings.

## ARGUMENT

### **I. THE TYPE OF LIMITED ISSUE RATE-MAKING SUGGESTED BY AQUILA IN ITS APPLICATION IS NOT PERMISSIBLE OUTSIDE OF THE CONTEXT OF A GENERAL RATE FILING AS PROVIDED FOR UNDER THE STATE NATURAL GAS REGULATION ACT.**

The Commission's statutory authority in matters relating to natural gas rates is set forth in the State Natural Gas Regulation Act, Neb. Rev. Stat. §§66-1801 through 66-1857 (Reissue 2003). For convenience, this legislation is hereinafter referred to as "the Act." The Act defines the term "general rate filing" as follows:

General rate filing means any filing which requests changes in overall revenue requirements for a jurisdictional utility.

Neb. Rev. Stat. §66-1801(7).

The Act also defines the term "rate" as follows:

Rate means every compensation, charge, fare, toll, tariff, rental, and classification, or any of them, demanded, observed, charged, or collected by any jurisdictional utility for any service.

Neb. Rev. Stat. §66-1801(12).

The Act provides for detailed procedures and requirements for general rate filings. See Neb. Rev. Stat. §66-1838. Aquila has clearly stated in its Application that it **does not** regard its Application as a request to initiate a general rate filing under Neb. Rev. Stat.

§66-1838. (See Aquila's Application, pages 1 and 3.) Aquila has also acknowledged in its Application that, in all general rate filings, the Commission is bound to follow the statutory process of review and approval of such general rate filings in accordance with §§66-1801(6) and 66-1838 of the Act. (See Aquila's Application, page 2.)

Aquila's Application seeks an increase in the overall revenue requirements for Aquila, as a jurisdictional utility, outside of the context of a general rate filing. Aquila suggests that such a proceeding should consider only certain categories of costs that the utility believes to be of types that typically increase over the passage of time, without also considering the full panoply of its costs that are considered and reviewed in the course of a general rate filing. Not only is this a departure from what the statutory language in the Act authorizes, but adoption of such an approach would have the negative effect of considering only a part of the costs of the utility without engaging in the corresponding consideration of all other costs, including those that may have decreased since the last general rate filing, that is inherent in a general rate filing.

The Public Advocate is certainly mindful of the fact that Aquila has advanced the argument that one of its reasons for filing its Application is "to avoid the time and expense on all parties required by the general rate filing statutes." (See Aquila's Application, page 3.) However, even if one were to assume for hypothetical purposes that the actual effect of the sort of limited cost recovery proposed by Aquila would be to avoid" the very "time and expense on all parties" to which Aquila refers, the threshold

legal issue would remain as to whether the Act provides statutory authority for the type of departure from the statutory general rate filing procedure that Aquila proposes.

Aquila states in its Application that “The Act provides for alternative rate making ability authority for actions other than a full blown rate proceeding.” (See Aquila’s Application, page 3.) Aquila further asserts that its “application for limited costs recovery is such an action.” However, the only specific provision of the Act that Aquila sees fit to quote in its Application as purported authority for its proposed “limited cost recovery” proceeding that could be a complete departure from the carefully considered structure of the Act is found in §66-1855, which provides that:

The commission may authorize, consistent with general regulatory principles, including, but not limited to . . . (2) mechanisms for the determination of rates by negotiation, and (3) customer choice and other programs to be offered by a natural gas public utility to unbundle one or more elements of the service provided by the utility.<sup>1</sup>

Whatever else Aquila’s proposed limited cost recovery proceeding may be, it most certainly is not a mechanism for “determination of rates by negotiation,” nor is it among the scope of “customer choice and other programs to be offered by a natural gas public utility to unbundle one or more elements of the service provided by the utility.” Aquila’s Application envisions the Commission having the ability to make an ultimate

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<sup>1</sup>Aquila does not quote or rely upon subsection (1) of §66-1855, which permits possible “banded rates with a minimum and maximum rate that allows the jurisdictional utility to offer ratepayers rates within the rate band for the purpose of attracting additional natural gas service demand or to retain such demand. The Public Advocate certainly agrees this subsection (1) does not apply to Aquila’s proposed limited cost recovery proceeding, but simply includes a reference to subsection (1) in this footnote to demonstrate that the language from §66-1855 that Aquila omitted from its quotation of the statute on pages 2 and 3 of its Application provides no support for Aquila’s Application.

determination whether to allow Aquila to recover additional revenue to cover whatever selected costs Aquila may choose to seek to recover, so it is not a proposal to permit rates to be determined by negotiation within the meaning of §66-1855(2). Likewise, Aquila's Application does not propose any sort of customer choice program or other program to "unbundle" one or more of the elements of the service provided by Aquila. This simply is not a situation in which a jurisdictional utility proposes a rate treatment whereby the transportation function (i.e., "trucking" gas to the customer) and the gas supply function (actually selling the gas commodity to the customer) would be divided, or "unbundled" – in fact there is no unbundling of any kind involved in Aquila's limited cost recovery proposal.

The Act does permit some rate changes to be considered outside the context of a general rate filing. See §66-1808, which specifically provides that its provisions do **not** apply to general rate filings. However, the provisions of §66-1808 are necessarily applicable only to proposed changes in rates or terms and conditions of service in those contexts in which the proposed change will not result in "changes in overall revenue requirements for a jurisdictional utility." §66-1802(6). If a change sought by a jurisdictional utility would result in a change in the overall revenue requirements for the utility, by definition, an application seeking such a change is a "general rate filing" within the meaning of §66-1802(6) and the Act's requirements for a "general rate filing" must be adhered to. This is the case regardless of how many purported policy arguments exist

as to why it might arguably be better to have a different procedure available for determination of rates for jurisdictional ratepayers.

The very reason that the Act provides for the detailed procedures and the related protections involved in general rate filings is to ensure that no “cherry picking” of issues occurs in cases in which a jurisdictional utility seeks an increase in its revenue requirements. Simple logic and fundamental fairness dictate that, rather than simply looking at selected costs that may have increased since the time an initial rate tariff was filed with the Commission or a revised tariff was established through the general rate filing procedure, the only truly fair way to determine whether there is a need for an increase in revenue is to conduct a detailed review of all costs – including both all costs that have increased and all costs that have decreased. Only in this way can a truly informed decision be made as to whether an increase in revenue should be allowed and, if so, the amount of such increase.

## **II. AQUILA’S LIMITED COST RECOVERY PROPOSAL IS CONTRARY TO PUBLIC POLICY.**

As noted in the preceding section of this brief, the statutory language of the State Natural Gas Regulation Act simply does not permit the Commission to consider a request for a rate change that involves a change in the overall revenue requirements of a jurisdictional utility other than through the “general rate filing” procedures provided for by the Act. Aquila has not been able to point in its Application to any other. This being the case, it simply doesn’t matter how compelling of a reason or set of reasons Aquila

may advance from a policy standpoint as to how Aquila contends it would be better if rates could be determined through the proposed limited cost recovery proceeding proposed in Aquila's Application. However, recognizing that Aquila has devoted a substantial part of its Application to such policy arguments, it is appropriate for the Public Advocate to point out that the procedure proposed in Aquila's Application is actually contrary to public policy.

It is undoubtedly true that a general rate case is a complex process that extends over a period of time. That is the very nature of the time-honored general rate case concept – the only way to make a truly informed and accurate determination of whether the utility's costs are such that a rate change may be required is to examine all pertinent costs – i.e., both costs that have increased and those that have decreased since the last rate determination. If only part of the costs would be looked at, whether at random or through some process where only a limited number of costs were selected for consideration, there is no assurance that the limited selection of costs picked will accurately reflect whether other costs have similarly changed. In fact, if one thinks about it for only a short period of time, it is readily apparent that very few costs incurred by a natural gas utility remain constant. Instead, by far the greater proportion of the costs changes over time, sometimes quite substantially, and such changes can be either increases in cost or decreases in cost. Surely, if a rate proceeding were to be proposed whereby only costs that have decreased since the last rate determination would be considered, the utility would vigorously oppose such a proposal as not providing a full and accurate picture of the overall costs of the

utility. The only way one can make a fair and reasonable change in the overall revenue requirements of a jurisdictional utility is to look at the overall costs of the utility.

Without limiting other respects in which the Public Advocate believes Aquila's Application is contrary to public policy, the Public Advocate presents the following points for the Commission's consideration:

1. Under the system whereby any changes in overall revenues of a jurisdictional utility can only be sought through a general rate filing, a utility must necessarily perform a cost/benefit analysis before it elects to file a general rate filing. Because significant human and monetary resources are necessarily required to file a general rate case, a utility should not (and most, do not) lightly file general rate cases. Instead, the theory of the general rate case is that a utility will only proceed to file general rate case when it feels there have been substantial enough increases in its overall costs to justify the expenditure of the time and money to make a general rate filing. If Aquila's Application would be approved and some sort of limited cost recovery proceeding were to be permitted, the utility would be relieved of having to conduct a cost/benefit analysis. In other words, the question that the general rate filing makes the utility answer of, "Will it be worthwhile to proceed with a general rate filing given what costs have gone up and what costs have gone down?" would be converted to the question of "What cost items do we think we can demonstrate increases in that would permit us to receive increased revenue without undergoing scrutiny of other costs items?" With all due respect, the

latter is **not** the right line of inquiry for utilities considering whether to initiate a general rate filing.

2. Contrary to the apparent suggestion of Aquila in its Application, it is not inevitable that every cost incurred by a jurisdictional utility will be borne by ratepayers. First, in virtually every general rate filing case, there will be categories of costs and/or specific costs within what might otherwise be appropriate categories that the Public Advocate will dispute as being proper cost items to be included in rates. However, even if we confine consideration for purposes of argument to the class of costs that everyone would agree constitute the types of costs that can justify a rate increase in appropriate circumstances in the context of a general rate filing, there is a critical time element that must not be lost. As time passes and as a utility incurs costs, the utility must (and certainly does) carefully consider whether the overall level of costs is such that the utility believes it is not being permitted to earn a fair rate of return on its rate base. However, just because one type of costs increases, even substantially, this does not mean that the overall costs of the utility are such that the revenues derived from rates are not great enough to still result in a good rate of return. Thus, if a utility incurs costs of a particular type in October of 2005 that may even represent a very substantial increase in the level of such costs from a prior period, the utility must still consider whether its overall costs – including both costs that have increased and costs that have decreased since the last rate determination – are sufficient to justify an increase in rates. If the utility decides **not** to initiate a general rate filing in October of 2005, even though there may have been an

increase in a particular category or type of cost in that time frame, the utility may not be able to recover that cost if it does not initiate a general rate filing until months or years into the future. By contrast, if some category or categories of costs are given the preferred treatment apparently sought by Aquila in its Application, this would translate into the utility receiving a virtually automatic increase in its overall revenue requirements for such types of costs, even if either the utility (in the context of the type of cost/benefit analysis noted in Item 1 above) or the Commission (in the context of a general rate filing) might otherwise determine that no increase was necessary to the utility's overall revenue requirements.

3. In every rate case, just as in virtually every other type of complex litigation, multiple issues are presented. For each side, some of these issues may be “winners” and some of these issues may be “losers.” Even among the “winners” and the “losers,” there are likely to be some issues that one party or the other may be more likely to prevail upon if the case is litigated to a contested outcome. A procedure that permits a party to “cherry pick” among issues to select only those more likely to be its “winners” is necessarily slanted – not only will this deprive the other party of the ability to attempt to negotiate a resolution of a contested rate case that may involve compromise by the party who feels it has more of a “winner” than a “loser” on various issues, but if a settlement cannot be reached, it deprives the decision-maker, in this case the Commission, from being able to survey all of the various issues presented and make the type of hard decisions that often have to be made in contested cases. In other words, both the parties and the Commission

may be deprived of the ability to find “a middle ground” to resolve groups of issues or even complete rate cases.

4. The only way to really know what has happened since the last rate determination to a utility’s overall costs is to perform a fully allocated cost of service study. The Public Advocate submits that performance of a fully allocated cost of service study is a practical requirement of a jurisdictional utility in a general rate filing if the utility hopes to meet its substantial burden of proof in such a general rate case. While admittedly a complex and time-consuming process, the very nature of a fully allocated cost of service study is to carefully consider all costs incurred by the utility in providing service to its customers and to properly allocate such costs among customer classes. Even if one accepts for purposes of argument a hypothetical instance in which all parties would agree that a utility’s revenue requirements should be increased to some degree, this would still leave unanswered the question of how such revenue increase should be implemented among different customer classes. Without a properly-conducted fully allocated cost of service study, allocation of revenue requirements increases among customers through higher rates is necessarily arbitrary.

The Public Advocate respectfully submits that (a) permitting increases in a jurisdictional utility’s revenue requirements shouldn’t occur without a properly-conducted fully allocated cost of service study; and (b) it is impossible to fairly allocate increases in rates to achieve increased revenue requirements among customer classes without a properly-conducted cost of service study. Aquila’s proposal in its Application

would permit substantial increases in the utility's revenue requirements without a fully allocated cost of service study – so not only will the true “net” of the utility's overall costs be unknown, but the Commission would be deprived of use of a tool necessary to fairly allocate increased revenue requirements among customer classes.

The Public Advocate is also aware that Aquila has asserted that permitting it to be awarded increases in its revenue requirements as suggested in Aquila's proposed limited cost recovery proceeding would save costs as compared to maintaining the current system under which revenue requirements can only be determined through a general rate filing. There is certainly no guarantee that any savings will actually be realized if Aquila's Application is granted. Even Aquila is limited to saying only that its proposal “may” result in reduced overall rate regulation costs. Moreover, there is simply no assurance that general rate cases will necessarily become more infrequent or cheaper if a limited cost recovery proceeding were to be permitted.

However, perhaps one of the most compelling public policy reasons against Aquila's proposal is the fact that no other jurisdiction has a procedure like the one specifically proposed by Aquila. Given the fact that centralized regulation of natural gas rates is still relatively new to Nebraska, this is not the time for the Commission to be the “first” to undertake a new and previously untested approach to rate-making that runs contrary to the time-honored principles and procedures of general rate cases.

**CONCLUSION**

For all of the foregoing reasons, the Public Advocate respectfully submits that Aquila's Application should be denied.

DATED this 7<sup>th</sup> day of October, 2005.

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## CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing was served by e-mail and by U.S. mail, sufficient postage prepaid this 7<sup>th</sup> day of October, 2005 upon Aquila, Inc. d/b/a Aquila Networks by serving same upon the following representatives of Aquila:

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